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SAPC-1160

16 June 1955

MEMORANDUM FOR THE RECORD

SUBJECT: Contract No. SC-21-54, Perkin-Elmer Corporation --
Project OCTROI -- Contract Negotiations

1. Definitive Contract No. SC-21-54 replaces Letter Contract No. SC-21-54. Letter Contract No. SC-21-54 was signed on 5 January 1955 and obligated the amount of \$2,500,000. Definitive Contract No. SC-21-54 obligates the amount of \$5,085,000.

2. Contract No. SC-21-54 is a fixed-price type contract with provisions for redetermining the contract cost at the time 75 percent of the target cost of \$4,745,000 has been expended in performance of the work. The contract, in Section L of the Schedule, states that the contract target cost is \$4,745,000 and the Contractor's target profit, corresponding to the target cost of \$4,745,000, is \$340,000. The contract target price, therefore, at the time the contract was signed was \$5,085,000. However, because of the unusual type equipment and services being procured under this contract and the delivery requirements placed on the Contractor, the Contractor would not agree to a normal Form IV type of price revision clause unless the Government agreed to an extraordinarily high maximum price because of the great risks which the Contractor visualized were inherent in this procurement. Accordingly, a compromise was reached wherein it was agreed that, at a given point (75% expenditure of the target cost of \$4,745,000), a review would be made of the expenditures incurred and additional expenditures expected to be incurred and a revision of the contract target cost would be made at that point, if necessary, to protect the Contractor with respect to reimbursement of actual costs of producing the items and services.

3. Contractor expects a profit of \$340,000 if the contract costs are in the near vicinity of \$4,745,000. However, if contract costs exceed \$4,745,000, provision is made for reducing the Contractor's profit to less than \$340,000. Conversely, if contract costs prove to be less than \$4,745,000, provision is made for increasing the

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Contractor's profit to more than \$340,000. No fixed schedule is provided for increasing or decreasing the profit, but this is left to negotiation of the parties after completion of the contract and in light of the circumstances which caused such increase or decrease in contract costs vis-a-vis the contemplated target cost at the time of signing of this contract.

4. Cost breakdown for this contract is as follows:

	<u>HYCON (Major Subcontractor)</u>	<u>P & E (Prime)</u>
Raw Costs	*	\$1,320,000
G & A, plus selling expenses	*	170,000,000 cost of appx 13%
Basic Costs	\$3,160,000	\$1,490,000
& E G & A on sub.	95,000** appx 3%	-----
Target Costs	\$3,255,000	\$1,490,000
		<u>\$4,745,000</u>
Profit	163,000 appx 5%	170,000 appx 12%
Target Prices	\$3,418,000	\$1,660,000
		<u>\$5,085,000</u>

SUMMARY

Target Cost	\$4,745,000
Target Profit (rounded to)	340,000 appx 7.16%
Target Price	\$5,085,000

* Hycon costs consist of raw costs plus a G & A of 8% (estimated) and a profit of 9%. This subcontract with Hycon by P & E will provide for an incentive type subcontract wherein Hycon obtains, in addition to a target profit of 9%, twenty percent (20%) of all savings from the target cost of such subcontract and is penalized on a sliding scale if the final costs exceed the target cost. Such penalty is made by reducing a portion of the excess cost from Hycon's target profit of 9%.

** The figure of \$95,000 although called G & A is actually an amount set up to cover all the operations of a separate office set up by P & E in Stamford, Connecticut, to house Dr. Roderic Scott, Chief Engineer of P & E who is the chief engineer and coordinator for the P & E - Hycon weapons system phase of the project. It is to defray the costs of liaison with the subcontractor and to provide security and is not

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subject to a separate overhead loading. Consideration will be given at the time of revision of the final price of this contract to allowing a larger amount for this service, provided the Contractor can show actual costs in excess of this figure attributable directly to such liaison service.

*** The G & A on the prime has been estimated at 13%, including approximately 1% for selling expense. With the inclusion of some \$1,320,000 of additional business to P & E, this G & A is expected to be lowered at the time of the next G & A redetermination. However, P & E plans to treat the subcontract differently since it is not in-plant work and carries a much lower profit. The subcontract will not be treated as "Sales" and consequently will not have gross company G & A expenditures spread against it. Should Government or company auditors insist on spreading total G & A against the subcontract, some relief may have to be given to P & E since the G & A on other Government business in the plant would be reduced without provision by P & E to recover it under the subcontract where no G & A as such is provided in the cost estimate. In other words, other Government agencies would benefit by a lower G & A against their work and Contract No. SC-21-54 would have to absorb the difference or the Contractor would have to absorb the difference as a loss of profit.

5. Contract No. SC-21-54 is Agency sterile but not Government sterile. It will be closely held at P & E and available only to a few cleared people. In addition to Contract No. SC-21-54, there exists a commercial agreement for this contract work between P & E and an Agency cut-out (see P & E payment plan). All billings, accounting, and other normal business procedures are documented under this commercial agreement and ostensibly the work is being performed by P & E for a commercial company. The work is known in the plant as the "Projector Project." The commercial agreement is only a cover to divorce the work from the Government to the greatest extent possible.

6. A similar arrangement will be made between P & E and Hycon. The legal document will be a contract containing necessary Government clauses but a cover commercial document will exist between P & E and Hycon to break the Government tie-up with the work. Hycon will account and bill under the cover document.

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7. Appendix I lists the items and services to be delivered under the contract. The prices for each item are billing prices and include the target profit of the subcontractor and the target profit of the prime contractor. Adjustment of these billing prices may be made from time to time; but final prices, including final profits, shall be determined in accordance with Section L, "Price Redetermination," of the Schedule.

8. The General Provisions of the contract are not unique, except that deletion and/or modification of some standard clauses has been made for security reasons. Also, certain alterations in the contract as written were agreed to before signature of the contract. (See "Alterations in Contract" clause.)

9. It is anticipated that certain additional work may be added hereunder, at which time the contract cost, profit and price will be altered accordingly, as well as the portions of the contract having to do with the description of the work.

Contract Negotiator

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